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292578—41——1

In the Supreme Court of the United States

OCTOBER TERM, 1940

No. —

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

THE CLEVELAND TRUST COMPANY, TRUSTEE OF THE TRUST ESTATE KNOWN AS GARFIELD BUILDING SITE TRUST

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT

The Solicitor General, on behalf of Guy T. Helvering, Commissioner of Internal Revenue, prays that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Sixth Circuit entered in the above cause on November 13, 1940.

OPINIONS BELOW

The opinion of the United States Board of Tax Appeals (R. 11–19) is reported in 39 B. T. A. 429. The opinion of the United States Circuit Court of Appeals for the Sixth Circuit (R. 111–115) is reported in 115 F. (2d) 481.

JURISDICTION

The judgment of the United States Circuit Court of Appeals was entered November 13, 1940 (R. 111). The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the taxpayer is an association taxable as a corporation, under Section 801 of the Revenue Act of 1934, as determined by the Commissioner, or is taxable merely as a pure trust, under Section 161 of the Revenue Act of 1934, as contended by the taxpayer and decided by the court.

STATUTES AND REGULATIONS INVOLVED

The pertinent statutes and regulations are set forth in the Appendix, *infra,* pp. 16–21.

STATEMENT

The respondent is trustee of a large business building the beneficial interest in which is divided into 535 shares, evidenced by transferable certificates which had been sold at public offering. The central issue is whether the enterprise may be taxed as an association rather than as a pure trust. The Board of Tax Appeals determined that the respondent was an association but the court below reversed. The facts as found in detail by the Board (R. 11–16) are as follows:

Prior to 1923, a 12-story building had been erected on the premises known as 322 Euclid Avenue, Cleveland, Ohio, which had been used by various institutions as banking quarters. As a result of a merger of the Cleveland Trust Company and the Garfield Savings Bank of Cleveland, the Cleveland Trust Company acquired the property by deed dated February 15, 1923. (R. 11.)

After that merger, the Cleveland Trust Company had no business use for the property. The State Banking & Trust Company desired to obtain the use of the premises for its banking quarters. Negotiations between these parties resulted in an agreement that the State Banking & Trust Company would pay to the Cleveland Trust Company the value of the building in cash and that the necessary further financing of its acquisition of the use of the premises would be arranged under what was locally known as land trust certificate financing. This plan was in general use in Cleveland, Ohio, and the vicinity, in financing real estate, as a substitute for the issuance of mortgage bonds in order to avoid double taxation under the then effective Ohio personal property tax law. Pursuant to that plan after payment of the value of the building in cash to the Cleveland Trust Company on November 15, 1924, the premises were leased to the State Banking & Trust Company for 99 years, the lease to be renewable in perpetuity. The lessee also received a 10-year option to buy the property for $550,000. (R. 11–12.)

Under the lease (R. 28–55), which provided for an annual rental of $30,000, the lessee was required to pay taxes, keep up insurance and maintain the building in good repair (R. 12).

Thereafter, and on the same day, the Cleveland Trust Company declared itself trustee of the fee of these premises, subject to the above-mentioned lease (R. 12).

The trust instrument (R. 64–77) provided that the petitioner held the described premises, subject to the lease, in trust, for the use and benefit of all present and future holders of certificates of equitable ownership therein; that the trustee would pay over quarterly to the record holders of the certificates their proportionate shares of rents or other income received by the trustee from the trust estate, after deducting the trustee's compensation and expenses; that the beneficial interests in the trust estate should be divided into 535 shares, evidenced by certificates of equitable ownership in the premises trusteed; that the trustee should keep suitable books of registration of such interests and the certificates representing them; that duplicate certificates should be issued upon proper proof of destruction or loss of such certificates; that no beneficiary should have any legal title to the trust property, real or personal, but only an equitable interest therein; that no beneficiary should have the right to call for a partition of the trust estate during the continu-

ance of the trust; that no transfer by operation of law of the interest of a beneficiary during the continuance of the trust should terminate the trust nor entitle the legal representative of a deceased beneficiary to an accounting or to any action in the courts or otherwise against the trust estate or the trustee, but that the executors, administrators, or assigns of any deceased beneficiary should succeed to the rights and be subject to the liabilities of the decedent; that notwithstanding any transfer by operation of law of any interest of a beneficiary, the trustee should be protected in his payment of distributions under the trust to the personal representative of any deceased beneficiary and that the rights of such a transferee should be enforceable against and binding upon such personal representative and not against the trustee or trust estate; that the compensation of the trustee for its services as such should be $575 annually, to be deducted from the rents collected by it, in addition to which it was authorized to incur necessary expenses in connection with the printing of the trust instrument, the certificates of equitable ownership, and such books and records as were necessary in connection therewith; that the trustee warranted neither the title to the premises nor the validity of the lease and did not guarantee its performance; that the trustee undertook to exercise only ordinary care in collecting and distributing rentals and carrying out and

distributing the proceeds of a sale; that the trustee should have the exclusive right to manage and control the estate as it deemed for the best interests of the beneficiaries, free from all control by the beneficiaries, as fully as though the trustee were the sole legal and equitable owner of the estate, and should not be subject to any obligations to the beneficiaries other than those especially assumed in the trust instrument; that the trustee could make agreements modifying, amending, or supplementing the lease in its sole discretion; that it could likewise settle claims either in contract or tort against it or the proceeds derived from the trust estate; that the trustee should be protected in acting upon any written document believed by it to be genuine and signed by the proper party; that the trustee should be indemnified from the trust estate for any personal liability incurred in the administration of the trust except such as arose from its personal and willful default; that the trustee should be exempt from liability for any act of commission or omission in the execution of the trust, so long as it acted in good faith, nor was it personally liable for such acts by any of its officers or employees though it was not obliged to give bond for the performance of the trust; that it could borrow funds to meet temporary exigencies in connection with the management of the trust estate but could not thereby bind either the trustee or the bene-

ficiaries personally; that the trustee could advise with legal counsel and the trustee should be protected in any bona fide action taken consistent with such advice; that the obligation of the trustee in the payment of money to the certificate holders was limited to the petitioner as trustee; that in the event of default by the lessee and the termination of the lease became necessary or advisable in the opinion of the trustee, notice should be given to the registered holders of certificates, upon which these holders had the right to advise the trustee whether the property should be offered for sale, or whether another lease thereof should be made, if possible; and, in the event of the failure of a majority in interest of the outstanding certificates to express their wishes, or, if the trustee should find, after making reasonable efforts, that it was impractical to comply with such wish of the certificate holders, the trustee should have full authority to sell, lease, manage, operate, or otherwise dispose of the premises, as it might deem advisable for the best interests of the certificate holders; that upon the exercise by the lessee of its option to purchase or upon the sale by the trustee, upon receipt of the purchase price, after deducting all necessary expenses, including reasonable compensation to the trustee for its services in connection with the completion of the sale, and the distribution of the net proceeds to the certificate holders, the trustee should distribute

such proceeds to the record certificate holders, and for successive trustees. (R. 12–14.)

It was contemplated that the annual rental of $30,000 to be received under the lease would be sufficient to yield to the holder of each $1,000 certificate into which the beneficiaries' interest in the estate was divided, an income of 5½% or $55 per year, after the payment of the trustee's fee, and, upon the exercise of the option to purchase by the lessee, the option price of $550,000 would be sufficient to distribute to each certificate holder approximately $1,028 (R. 14).

The certificates of beneficial ownership were delivered to and sold by the Cleveland Trust Company at $1,000 per certificate. The prospectus issued by that company recited that the land had been appraised at $550,000 and the building at $455,000. Each certificate was entitled "Trustee's Certificate of Equitable Interest The Garfield Lot," and recited that its holder was an owner of a $\frac{1}{535}$ of the beneficial interest and ownership in such premises, which were described in detail, and entitled to receive the rents and profits therefrom during the continuance of the trust, as provided in the trust agreement. The certificate further recited that the premises were subject to a 99-year lease, renewable in perpetuity; that the trustee would pay over to the certificate holder his proportionate share of the rents and proceeds from the sale of the trust estate and that the certificate was transferable. (R. 14.)

The certificate holders had no organization among themselves and never held any meetings (R. 14).

The State Banking & Trust Company, lessee, was thereafter merged into the Union Trust Company of Cleveland, which assumed its obligations as such lessee. In March 1933, a conservator was appointed for the Union Trust Company, and about June 15, 1933, the superintendent of banks of the State of Ohio took over possession of the assets of the Union Trust Company for liquidation, that institution having been determined to be insolvent. (R. 14–15.)

There was no default in the lease until after the appointment of the conservator for the Union Trust Company. Upon that default, the taxpayer, about July 6, 1933, retained counsel for the purpose of collecting delinquent rentals and advising the trustee with respect to its rights in the situation occasioned by the closing of the Union Trust Company. The superintendent of banks of Ohio, in charge of the liquidation of that company, commenced an action in the Common Pleas Court of Cuyahoga County, Ohio, to abandon the lease which had been assumed by the Union Trust Company. In that action, the taxpayer asserted that the superintendent of banks had no legal right to abandon the lease. This action was settled on March 15, 1934, by the payment of $75,000 to the taxpayer by the superintendent of banks

of Ohio, as such liquidator, the release by taxpayer of the superintendent of banks from all claims and liabilities because of the lease, and the assignment to Three Twenty-two Euclid, Incorporated, with the consent of the trutsee. (R. 58–63.) This corporation was newly formed by petitioner, all the stock of which was held by a nominee of the petitioner, for the benefit of the trust. Three Twenty-two Euclid, Incorporated, never had any salaried officers or employees. Its officers and directors were officers or employees of the Cleveland Trust Company and its books of account were kept by an officer of the Cleveland Trust Company. This new corporation was organized for the purpose of taking over the leasehold estate and to preserve its continuity until another long-term tenant for the property could be obtained. (R. 15.)

Under lease dated January 25, 1935 (R. 77–88), and later modified as of April 16, 1936 (R. 91–95), Three Twenty-two Euclid, Incorporated, leased the entire premises to Lerner Shops of Ohio, Incorporated, for 20 years. This lease provided for an annual rental of $35,000 for the first 10 years and $40,000 for the last 10 years; with the demolition of the building then on the property and the construction of a new building suitable to the needs of the lessee, to the construction of which the lessee should contribute $25,000. The new building was constructed under a general contract between Three

Twenty-two Euclid, Incorporated, and the George Rutherford Company, at a total cost of approximately $135,000, of which $25,000 was paid by the lessee and the remainder by Three Twenty-two Euclid, Incorporated, partially out of its own funds and the balance financed by the taxpayer. (R. 15–16.)

Prior to the execution of the lease with the Lerner Shops of Ohio, Incorporated, the collection of rents from the two tenants then occupying the premises was made by the Cleveland Trust Company. Expenses incident to the maintenance of those portions of the premises not occupied by the two sublessees were, during that period, paid by the Cleveland Trust Company, and were only such as were necessary to preserve the property pending the finding of a long-term lessee. After the construction and occupancy of the new building, the rent was paid to Three Twenty-two Euclid, Incorporated, and that corporation paid to the taxpayer the rental on the original 99-year lease. Except for the activities detailed, neither the taxpayer nor Three Twenty-two Euclid, Incorporated, engaged in any other material activities during the several years mentioned, including that of 1934, except the collection and distribution of rentals to the certificate holders. (R. 16.)

The taxpayer reported the income received and distributed to the certificate holders during the year 1934 on a fiduciary income tax return and paid

a tax on undistributed income of the trust for that year in the amount of $799.77. During the year 1934, the taxpayer received no income other than the item of $75,000, mentioned above, which was received in settlement on the litigation occurring upon default in the original lease. During that year, the taxpayer distributed to certificate holders the sum of $29,425. (R. 16.)

The Board concluded (R. 16–19) that the taxpayer was an association taxable as a corporation, but the court below reversed (R. 111–115).

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In holding and deciding that the taxpayer was taxable as a trust under Section 161 of the Revenue Act of 1934, *infra*.

2. In failing to hold and decide that the taxpayer was an association taxable as a corporation.

3. In reversing the order of the Board of Tax Appeals.

REASONS FOR GRANTING THE WRIT

1. The decision of the court below is in conflict with *Title Insurance & Trust Co.* v. *Commissioner,* 100 F. (2d) 482 (C. C. A. 9th), where the court reached the opposite conclusion upon substantially identical facts. There, as here, a bank, as owner of a 12-story office building, had arranged for a 99-year lease and almost simultaneously with the execution of the lease had placed

the fee of the premises in trust. In both cases, provision was made for certificates of beneficial interest (665 in the *Title Insurance & Trust Co.* case and 535 in the instant case). In both cases, the certificates were transferable and continuity of the trust was not to be affected by death of the beneficial owners. Both the trustees and the certificate holders were protected against personal liability. In addition to the primary function of collecting and disbursing the rentals, the trustees in both cases were empowered, in case of default by the lessee, to take appropriate steps for the protection of the certificate holders, including the power to borrow money and execute securities as well as to lease, operate, sell, or otherwise dispose of the trust property.[1]

2. The decision of the court below is in substantial conflict with the decision of this Court in *Swanson* v. *Commissioner,* 296 U. S. 362. The court below, in ruling that the taxpayer was a pure trust rather than an association, stated that (R. 115): "The trust instrument shows no plan to carry on a business in buying, selling, leasing or dealing in real estate." But in the *Swanson* case, where the trust property consisted of only one

[1] The only material difference lies in the fact that here there was actually a default, giving rise to the trustee's exercise of the broad powers of management during the tax year in question, but that difference makes the case at bar even stronger for the Government than the *Title Insurance & Trust Co.* case.

apartment house, this Court pointed out that no other real estate dealings need be shown. It is also pertinent to observe that in the *Swanson* case, as in the instant case, the rents were actually collected for the trustee by an agent.

3. The question here presented is one of general importance. As observed by the court below (R. 112), this type of trust is in general use in Ohio, and it is probably employed to a considerable extent outside of Ohio, as well. It is important to the administration of the revenue acts that the application of the general principles established by such cases as *Morrissey* v. *Commissioner,* 296 U. S. 344, and *Swanson* v. *Commissioner, supra,* to such a frequently recurring *type* of organization as is here presented be authoritatively settled.

We do not have here merely an individual case calling for the application of established principles. In such circumstances, the Government does not normally seek review in this Court and it opposes petitions for certiorari filed by others. But here there is involved a type of organization in wide use, and a misapplication of established principles affecting the administration of the revenue law with respect to a large number of taxpayers is a matter of importance, particularly when two circuit courts of appeals have reached opposite conclusions upon substantially identical sets of facts.

CONCLUSION

Therefore, it is respectfully submitted that this petition for a writ of certiorari should be granted.

FRANCIS BIDDLE,
Solicitor General.

FEBRUARY 1941.

APPENDIX

Revenue Act of 1934, c. 277, 48 Stat. 680:

SEC. 161. IMPOSITION OF TAX.

(a) *Application of Tax.*—The taxes imposed by this title upon individuals shall apply to the income of estates or of any kind of property held in trust, including—

* * * * *

(2) Income which is to be distributed currently by the fiduciary to the beneficiaries, and income collected by a guardian of an infant which is to be held or distributed as the court may direct;

* * * * *

[U. S. C., Title 26, Sec. 161.]

SEC. 162. NET INCOME.

The net income of the estate or trust shall be computed in the same manner and on the same basis as in the case of an individual, except that—

* * * * *

(b) There shall be allowed as an additional deduction in computing the net income of the estate or trust the amount of the income of the estate or trust for its taxable year which is to be distributed currently by the fiduciary to the beneficiaries, and the amount of the income collected by a guardian of an infant which is to be held or distributed as the court may direct, but the amount so allowed as a deduction shall be included in computing the net income of the beneficiaries whether distributed to them or not. Any amount allowed as a deduction under this paragraph shall not

be allowed as a deduction under subsection (c) of this section in the same or any succeeding taxable year;

* * * * *

[U. S. C., Title 26, Sec. 162.]

SEC. 801. DEFINITIONS.

(a) When used in this Act—

* * * * *

(2) The term "corporation" includes associations, joint-stock companies, and insurance companies.

* * * * *

[U. S. C., Title 26, Sec. 1696.]

Treasury Regulations 86, promulgated under the Revenue Act of 1934:

ART. 801–1. *Classification of taxables.*— For the purpose of taxation the Act makes its own classifications and prescribes its own standards of classification. Local law is of no importance in this connection. Thus a trust may be classed as a trust or as an association (and, therefore, as a corporation), depending upon its nature or its activities. (See article 801–3.) The term "partnership" is not limited to the common law meaning of partnership, but is broader in its scope and includes groups not commonly called partnerships. (See article 801–4.) The term "corporation" is not limited to the artificial entity usually known as a corporation, but includes also an association, a trust classed as an association because of its nature or its activities, a joint-stock company, an insurance company, and certain kinds of partnerships. (See articles 801–2 and 801–4.) The definitions, terms, and classifications as set forth in section 801, shall have the same respective meaning and scope in these regulations.

ART. 801–2. *Association.*—The term "association" is not used in the Act in any narrow or technical sense. It includes any organization, created for the transaction of designated affairs, or the attainment of some object, which, like a corporation, continues notwithstanding that its members or participants change, and the affairs of which, like corporate affairs, are conducted by a single individual, a committee, a board, or some other group, acting in a representative capacity. It is immaterial whether such organization is created by an agreement, a declaration of trust, a statute, or otherwise. It includes a voluntary association, a joint-stock association or company, a "business" trust, a "Massachusetts" trust, a "common law" trust, an "investment" trust (whether of the fixed or the management type), an interinsurance exchange operating through an attorney in fact, a partnership association, and any other type of organization (by whatever name known) which is not, within the meaning of the Act, a trust or an estate, or a partnership. If the conduct of the affairs of a corporation continues after the expiration of its charter, or the termination of its existence, it becomes an association.

ART. 801–3. *Association distinguished from trust.*—The term "trust," as used in the Act, refers to an ordinary trust, namely, one created by will or by declaration of the trustees or the grantor, the trustees of which take title to the property for the purpose of protecting or conserving it as customarily required under the ordinary rules applied in chancery and probate courts. The beneficiaries of such a trust generally do no more

than accept the benefits thereof and are not the voluntary planners or creators of the trust arrangement. Even though the beneficiaries do create such a trust, it is ordinarily done to conserve the trust property without undertaking any activity not strictly necessary to the attainment of that object.

As distinguished from the ordinary trust described in the preceding paragraph is an arrangement whereby the legal title to the property is conveyed to trustees (or a trustee) who, under a declaration or agreement of trust, hold and manage the property with a view to income or profit for the benefit of beneficiaries. Such an arrangement is designed (whether expressly or otherwise) to afford a medium whereby an income or profit-seeking activity may be carried on through a substitute for an organization such as a voluntary association or a joint-stock company or a corporation, thus obtaining the advantages of those forms of organization without their disadvantages.

If a trust is an undertaking or arrangement conducted for income or profit, the capital or property of the trust being supplied by the beneficiaries, and if the trustees or other designated persons are, in effect, the managers of the undertaking or arrangement, whether the beneficiaries do or do not appoint or control them, the beneficiaries are to be treated as voluntarily joining or cooperating with each other in the trust, just as do members of an association, and the undertaking or arrangement is deemed to be an association classified by the Act as a corporation.

By means of such a trust the disadvantages of an ordinary partnership are avoided, and the trust form affords the ad-

vantages of unity of management and continuity of existence which are characteristic of both associations and corporations. This trust form also affords the advantages of capacity, as a unit, to acquire, hold, and dispose of property and the ability to sue and be sued by strangers or members, which are characteristic of a corporation; and also frequently affords the limitation of liability and other advantages characteristic of a corporation.

These advantages which the trust form provides are frequently referred to as resemblance to the general form, mode or procedure, or effectiveness in action, of an association or a corporation, or as "quasi-corporate form." The effectiveness in action in the case of a trust or of a corporation does not depend upon technical arrangements or devices such as the appointment or election of a president, secretary, treasurer, or other "officer," the use of a "seal," the issuance of certificates to the beneficiaries, the holding of meetings by managers or beneficiaries, the use of a "charter" or "by-laws," the existence of "control" by the beneficiaries over the affairs of the organization, or upon other minor elements. They serve to emphasize the fact that an organization possessing them should be treated as a corporation, but they are not essential to such classification, for the fundamental benefits enjoyed by a corporation, as outlined above, are attained, in the case of a trust, by the use of the trust form *itself*. The Act disregards the technical distinction between a trust agreement (or declaration) and ordinary articles of association or a corporate charter, and all other differences of detail. It treats such a trust according to

its essential nature, namely, as an association. This is true whether the beneficiaries form the trust or, by purchase or otherwise, acquire an interest in an existing trust.

The mere size or amount of capital invested in the trust is of no importance. Sometimes the activity of the trust is a small venture or enterprise, such as the division and sale of a parcel of land, the erection of a building, or the care and rental of an office building or apartment house; sometimes the activity is a trade or business on a much larger scale. The distinction is that between the activity or purpose for which an ordinary strict trust of the traditional type would be created, and the activity or purpose for which a corporation for profit might have been formed.

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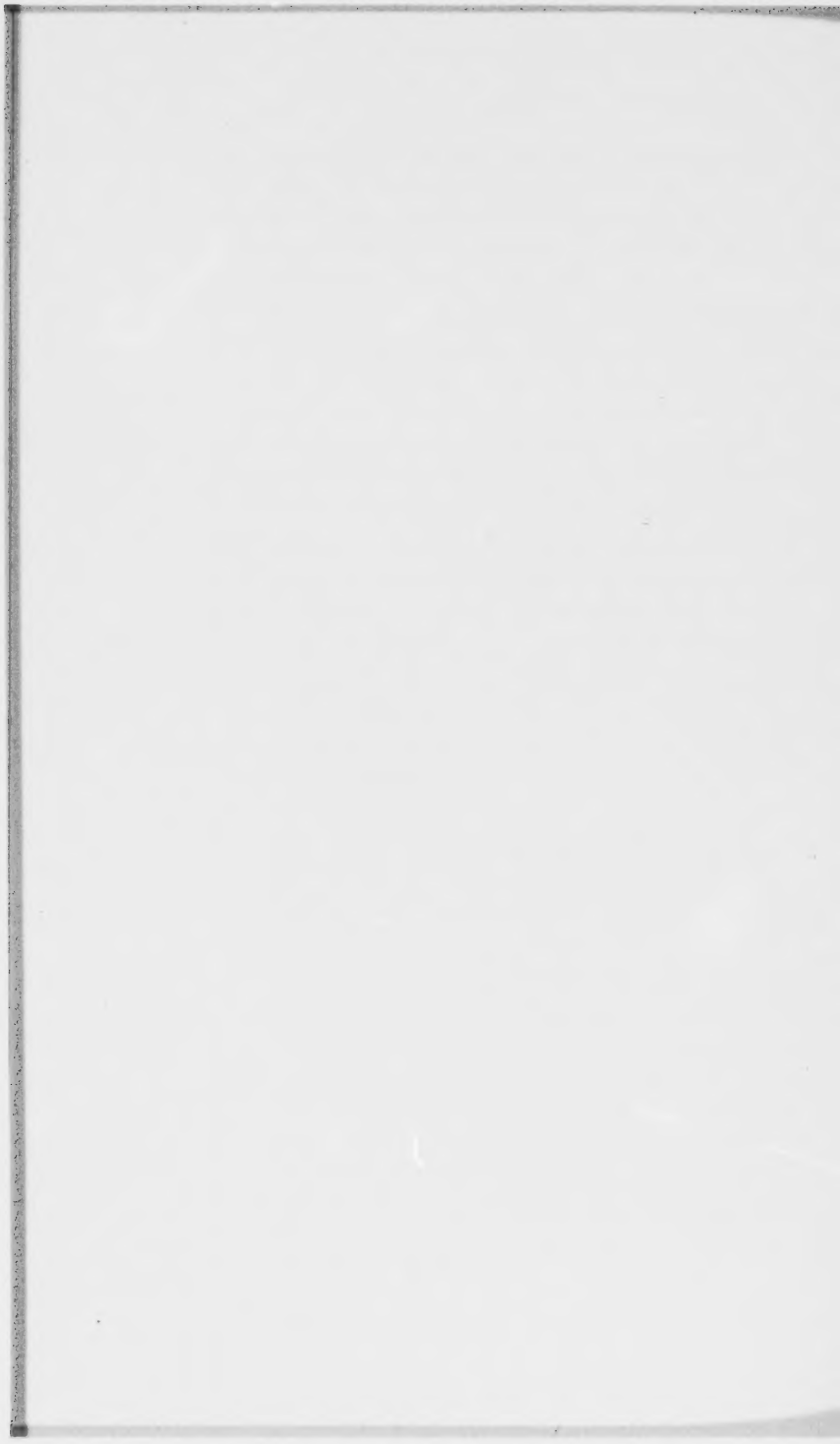

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In the Supreme Court of the United States

OCTOBER TERM—1940.

No. 764.

COMMISSIONER OF INTERNAL REVENUE,
Petitioner,

vs.

THE CLEVELAND TRUST COMPANY,
Trustee of the Trust Estate known as
Garfield Building Site Trust,
Respondent.

On Petition for Writ of Certiorari
To The United States Circuit Court of Appeals
For the Sixth Circuit.

BRIEF OF RESPONDENT IN OPPOSITION.

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2. The decision of the court below is not in conflict with the decision of this Court in Swanson vs. Commissioner, 296 U. S. 362, but properly applies the principles there established 6

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Respondent.

On Petition for Writ of Certiorari
To The United States Circuit Court of Appeals
For the Sixth Circuit.

BRIEF OF RESPONDENT IN OPPOSITION.

STATEMENT.

The question presented and the facts involved are correctly set forth in the petition for the writ.

In essence the facts disclose that the respondent is the trustee of a trust created as an integral part of an issue of land trust certificates in the ordinary form. The arrangement is similar in all respects to that recently considered by this Court in *Helvering vs. F. & R. Lazarus & Company,* 308 U. S. 252, in which the Court held that a land trust certificate issue is, for purposes of Federal income taxation, to be considered as the equivalent of a mortgage bond issue. The sole question is whether a trust created for so specific and limited a purpose is taxable as a trust or as an association.

SUMMARY OF ARGUMENT AGAINST ISSUANCE OF WRIT.

1. There is no conflict between the decision of the court below and the decision of the Circuit Court of Appeals for the Ninth Circuit in *Title Insurance & Trust Company vs. Commissioner,* 100 Fed. (2d) 482.

2. The decision of the court below is not in conflict with the decision of this Court in *Swanson vs. Commissioner,* 296 U. S. 362, but properly applies the principles there established.

3. The question here presented is not one of general importance but involves only the application of principles recently established by this Court to a specific type of real estate financing.

ARGUMENT.

Since 1913 this Court has on various occasions considered the characteristics which distinguish a strict trust from the type of entity which, although in the trust form, is subject to Federal income taxation as an association. After passing through two stages, represented by the decisions of this Court in *Crocker vs. Malley,* 249 U. S. 223, and *Hecht vs. Malley,* 265 U. S. 144, the general question was again considered and finally determined in a group of cases decided December 16, 1935. *Morrissey vs. Commissioner,* 296 U. S. 344; *Swanson vs. Commissioner,* 296 U. S. 362; *Helvering vs. Combs,* 296 U. S. 365; *Helvering vs. Coleman-Gilbert Associates,* 296 U. S. 369.

In these cases, this Court stated that it was impossible "in the nature of things to translate the statutory concept of 'association' into a particularity of detail that would fix the status of every sort of enterprise or organization which ingenuity may create." Nevertheless, the Court found the need of further examination of the question and adopted the fundamental test that before an association can exist there must be the entering into of a joint enterprise for the transaction of business. Throughout the

opinion, references to this fundamental requirement of "carrying on a business enterprise" occur. The Court carefully distinguished between two fundamentally different types of organization: the association, the object of which is to provide a medium for the conduct of a business and the sharing of its gains, and the trust, the object of which is to hold and conserve particular property, with incidental powers.

Since the decision in these cases, the courts have uniformly applied the principles therein enunciated and have considered the law as settled. The court below in its decision recognized and applied these principles and held that the nature and purpose of the trust here involved was foreign to any concept of carrying on business for profit and the sharing of its gains, and, therefore, properly determined that the trust was taxable as a trust.

In support of its petition for a writ of certiorari, the petitioner contends that the decision below is in conflict with *Title Insurance & Trust Company vs. Commissioner, supra,* that the decision below is in substantial conflict with the decision of this Court in *Swanson vs. Commissioner, supra,* and that the question here presented is one of general importance. It is submitted that a consideration of the reasons thus advanced by the petitioner indicates no basis for the granting of certiorari.

1. There is no conflict between the decision of the court below and the decision of the Circuit Court of Appeals for the Ninth Circuit in Title Insurance & Trust Company vs. Commissioner, 100 Fed. (2d) 482.

While it is true that *Title Insurance & Trust Company vs. Commissioner, supra,* involved a trust which was on its face rather similar to that here involved, that decision is clearly distinguishable. In that case, at the time the trust was created, *the property was not subject to any outstanding lease.* The trustee was authorized, but not required,

to lease the trust property or any part of it to a named corporation for a stated rental and to grant to the lessee an option to purchase the property. In the *Title Insurance & Trust Company* case the court stated (page 485):

> "In *Crocker vs. Malley*, 249 U. S. 223, 39 S. Ct. 270, 63 L. Ed. 573, 2 A. L. R. 1601, cited by petitioner, the function of the trustees was simply to collect the rents and income of the trust property. In this case, the function of the trustee was not so limited. Here, the trustee was empowered to lease the whole or any part of the trust property and, in 1927, did lease the whole of it to Sun Realty Company."

The decision of the court thus provides the fundamental distinction between that case and the one here presented, *where the property, when conveyed to the trustees, was already subject to a ninety-nine year lease and the lease was expressly made a part of the trust agreement by reference.* In the present case, at the time of the creation of the trust, the outstanding lease restricted the trustee in its powers and authorities as effectively as though its activities had been limited to the collection and disbursement of rentals by an express provision contained in the declaration of trust. This distinction is of vital importance in view of the test laid down by this Court in *Morrissey vs. Commissioner, supra,* which emphasized throughout the opinion that entering into a "business enterprise" is an essential characteristic of an association.

Whether the Circuit Court of Appeals for the Ninth Circuit should have taken so technical a view of the financing plan involved in *Title Insurance & Trust Company vs. Commissioner, supra,* is debatable, but it is unnecessary to consider that question in view of the clear basis of distinction which the court itself provides.

It is important to point out, moreover, that the *Title Insurance & Trust Company* case has lost its force as a precedent by the subsequent decision of this Court in *Helvering vs. F. & R. Lazarus & Company,* 308 U. S. 252.

The *Title Insurance & Trust Company* case was decided over two years ago, on December 27, 1938. On December 4, 1939, this Court entered its opinion in the *Lazarus* case, which involved the question of whether the lessee of property, which was the subject of land trust certificate financing of the type here presented, was entitled to deduct depreciation upon buildings located on the land. This Court held that such financing arrangements are to be considered as equitable mortgages for purposes of the Federal income tax. The basis for the decision is apparent from the following quotation from the opinion (page 255):

> "We think the Board justifiably concluded from its findings that the transaction between the taxpayer and the trustee bank, in written form a transfer of ownership with a lease back, was actually a loan secured by the property involved. General recognition has been given the 'established doctrine that a court of equity will treat a deed, absolute in form, as a mortgage, when it is executed as security for a loan of money.' In the field of taxation, administrators of the laws, and the courts, are concerned with substance and realities, and formal written documents are not rigidly binding. Congress has specifically emphasized the equitable nature of proceedings before the Board of Tax Appeals by requiring the Board to act 'in accordance with the rules of evidence applicable in courts of equity of the District of Columbia.' 26 U. S. C. 611."

This decision, as applied to the case here under consideration, would indicate that, for income tax purposes, the lessee corporation is to be regarded as the owner of the property, and the trustee is to be regarded as occupying the same position as a trustee under a bond issue. Completing the analogy, the beneficiaries of the trust are to be regarded as bondholders, and the essential nature of the land trust certificate plan of financing is to be regarded as a substitute for a mortgage bond issue. Thus considered, there is no real venture or "business enterprise," which is a pre-requisite for the taxation of a trust as an

association. As the court below stated, there is no body of persons acting together in the prosecution of a business enterprise for profit.

An examination of the briefs filed in the *Title Insurance & Trust Company* case discloses that this point was not brought to the attention of the court. Certain it is that the Circuit Court of Appeals for the Ninth Circuit did not have the benefit of the subsequent decision of this Court in the *Lazarus* case.

It would appear that the decision of the Circuit Court of Appeals for the Ninth Circuit in the *Title Insurance & Trust Company* case is no longer of importance as an authority in view of the Supreme Court's subsequent decision in the *Lazarus* case. Accordingly any possible conflict between the two decisions is not of sufficient importance to deserve the further attention of this Court, whose prior decisions have so clearly confirmed the correctness of the decision below.

2. The decision of the court below is not in conflict with the decision of this Court in Swanson vs. Commissioner, 296 U. S. 362, but properly applies the principles there established.

The petitioner also urges that the decision below is in substantial conflict with the decision of this Court in *Swanson vs. Commissioner, supra.* While it is difficult to discuss this decision and at the same time avoid a consideration of the merits, it should be observed that the only vital point of resemblance to which the petitioner alludes is the fact that in both cases the property held consisted of a single parcel of real estate. In the *Swanson* case, vacant land had been acquired by two individuals with the view of improving it by the erection of an apartment house. After the apartment house had been constructed, the property was, at the suggestion of the owners' attorney, conveyed to trustees who issued receipts to evidence the interests of

the beneficiaries, representing 1,000 shares at the par value of $100.00 each. These shares were issued to the two owners of the land, who later transferred them to their wives. The agreement there clearly contemplated the continuance by the trustee of a business enterprise theretofore carried on by the creators of the trust. The petitioner implies in his brief that the court below, in concluding that there was present no plan to carry on a business, relied upon the fact that a single building was involved. That implication is not warranted by the court's opinion, which clearly points out that the whole plan and purpose of land trust financing are alien to the accepted concept of a business enterprise for profit.

The opinion of the court below is not, therefore, in conflict with the decision of this Court in *Swanson vs. Commissioner.* On the contrary, the decision expressly recognized and followed the principles established in the *Swanson* case (R. 115) and applied those principles to an arrangement which this Court had theretofore analyzed for income tax purposes in the *Lazarus* decision.

3. The question here presented is not one of general importance but involves only the application of principles recently established by this Court to a specific type of real estate financing.

The petitioner also contends that the question presented is one of general importance. As indicated in the petitioner's brief, this type of financing was probably employed most extensively in Ohio where the confiscatory taxation of real estate and mortgages under former Ohio laws gave added impetus to its use. The Revenue Agent's report tentatively proposing a deficiency in the present case was dated December 17, 1936. (R. 8.) Although over four years have now elapsed, an investigation at the three large Cleveland trust companies (corporate trustees almost invariably acted as trustees under the land trust issues) dis-

closes only three pending cases, in addition to this one, which involve the taxation of such trusts as associations. The deficiencies in tax ordinarily in issue when such an attempt is made are small. The size of the deficiency in the present case is small, but is larger than usual because of the fact that the trustee received a large amount of income upon a settlement with the defaulting lessee. (R. 16.) If the question of general importance is to be gauged by such tests, the question here presented is more properly characterized as one of infrequent occurrence, involving unimportant deficiencies, and of less general interest than the ordinary income tax question.

Moreover, the history of the treatment of such trusts by the Treasury Department is of interest in considering the general importance of the question. As early as March 10, 1925, the Solicitor of the Treasury Department ruled in an unreported decision (S. M. 3206), in answer to an inquiry by the trustee of a similar trust, that such a trust was to be taxed as a strict trust and not as an association. Thereafter, the same conclusion was reached in a ruling published in the bulletin service in 1928 as G. C. M. 1940-VII-1 C. B. 46. Until the question was raised in the present case and in the *Title Insurance & Trust Company* case, it is believed that the Department consistently followed its early decisions. In view of this uniform treatment, which accords with the conclusion reached by the court below, and in view of the relatively few instances in which the question has arisen in a city which is generally regarded as the home of land trust certificate financing, it would seem that the question presented is not one of general importance.

CONCLUSION.

The foregoing discussion indicates an absence of any conflict between the decision below and cases decided by this Court or by any Circuit Court of Appeals. The question is one calling only for the application of principles recently established by this Court in *Morrissey vs. Commissioner, supra,* and other cases decided the same day, and in *Helvering vs. F. & M. Lazarus & Co., supra.* The principles there laid down are not questioned, limited, or misinterpreted by the court below but were reiterated and properly applied to the facts presented.

It is, therefore, respectfully submitted that the petition for a writ of certiorari should be denied.

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